TEXACO, INC.

IBLA 93-566 Decided March 25, 1996

Appeal from a decision by the Acting Deputy Director, Minerals Management Service, denying a request for refund of royalties assessed
for flared gas. MMS 86-0343-O&G.

Affirmed.

1. Oil and Gas Leases: Generally--Oil and Gas Leases: Royalties

NTL-4A replaced provisions of NTL-4 which had changed the long-standing Departmental policy that a royalty would not be assessed for oil or gas that is unavoidably lost or used in lease operations. It did not alter or amend the Department's long-standing policy that the Government should be compensated for gas that was vented or flared without prior approval of the Supervisor or avoidably lost. A request for refund of royalties paid for gas flared during the period between the issuance of NTL-4 and NTL-4A will be denied if there is no showing that the Supervisor had given prior approval or that the gas had been unavoidably lost.

APPEARANCES: Brian L. Mullin, Esq., Denver, Colorado, for Texaco, Inc.; Peter J. Schaumberg, Esq., Howard W. Chalker, Esq., Geoffrey Heath, Esq., Office of the Solicitor, U.S. Department of the Interior, Washington, D.C., for the Minerals Management Service.

OPINION BY ADMINISTRATIVE JUDGE MULLEN

Texaco, Incorporated (Texaco) has appealed a February 23, 1993, decision by the Acting Deputy Director, Minerals Management Service (MMS), denying Texaco's request for refund of $37,665.25 paid during the period 1975 to 1977 as royalties for gas flared at Federal oil and gas leases. The basis for the denial was that Texaco did not qualify for a refund of royalties pursuant to NTL-4A. 1/

1/ Notice to Lessees and Operators of Onshore Federal and Indian Oil and Gas Leases No. 4A, 44 FR 76600 (Dec. 27, 1979), effective Jan. 1, 1980.

Texaco paid the royalties in question after December 1, 1974, the effective date of the Notice to Lessees and Operators of Federal Onshore Oil and Gas Leases-Royalty Payment on Oil and Gas Lost (NTL-4), issued on November 15, 1974. NTL-4 provided that from and after December 1, 1974, gas vented or flared in a well test and gas otherwise vented or flared with prior written authorization from the Area Oil and Gas Supervisor would be gas production subject to a royalty. 2/ This notice deviated from a long-standing Departmental interpretation of the Mineral Leasing Act, 30 U.S.C. §§ 181-287 (1994), that gas which was vented or flared by a lessee was not subject to a royalty if the lessee had gained prior approval of the venting or flaring.

The validity of NTL-4 was challenged by numerous oil and gas producers. In Marathon Oil Co. v. Andrus, 452 F. Supp. 548 (D. Wyo. 1978), the court held that the Department's contemporaneous construction of the original language of section 17 of the Mineral Leasing Act and the 1946 amendments to the effect that royalties would not be levied on oil or gas which was unavoidably lost or used in lease operations was entitled to great weight, particularly in light of subsequent congressional ratification of that interpretation. The court then struck down the conflicting provisions of NTL-4 as arbitrary, capricious, and an abuse of discretion.

Following this judicial rejection of portions of NTL-4, the Department ceased seeking payment of royalties on oil used in production and unavoidably lost gas and promulgated NTL-4A. See 44 FR 76600 (Dec. 27, 1979). In this Federal Register notice the Department acknowledged that certain provisions of NTL-4 had been revoked and stated that those provisions would be superseded by NTL-4A. The Federal Register notice also advised lessees and operators who had submitted royalty payments under the revoked provisions of NTL-4 that they could apply for refund of those payments. The addendum to NTL-4A specified the application requirements and how refunds would be approved and processed.

On July 31, 1980, Texaco filed for refund of $37,665.25 in royalties paid from 1975 to 1977 for gas flared on 20 Federal leases. On May 7, 1986, the Houston Area Compliance Office denied Texaco's refund request because the gas had been avoidably lost and flared without prior permission. The Houston Office decision noted that on several occasions MMS had asked Texaco to either submit documents indicating that an authorized officer had approved the flaring or demonstrate that the gas was unavoidably lost, but that Texaco had tendered neither. Texaco appealed to the Director, MMS.

2/ NTL-4 also provided that, if written authorization was not obtained prior to venting or flaring gas, the gas was considered to be avoidably lost, and the United States was to be compensated for its full value.

In Lewis Energy Corp., MMS-83-0038-O&G (Oct. 16, 1987), the Director, MMS, remanded a number of appeals, including Texaco's, to the MMS Royalty Management Program to await Bureau of Land Management (BLM) review to determine whether the appellants were entitled to a refund. After reviewing its Texaco files, BLM concluded that Texaco had not gained permission to flare or vent the gas it had flared during the 1975 to 1977 period. BLM also noted that it could find no correspondence retroactively approving the flaring, or any evidence that the losses were unavoidable. 3/ On February 23, 1993, the Acting Deputy Director affirmed the Houston Area Compliance Office decision. Texaco appealed to this Board.

On appeal, Texaco does not contend that it was uneconomic to recover the gas, that the gas was unavoidably lost, or that the Area Oil and Gas Supervisor had approved the flaring. It argues that, when MMS refused to grant a refund, MMS ignored the Marathon decision and attempted "to impose certain requirements on Texaco that were similar to the same requirements of NTL-4 invalidated by the Marathon decision" (Statement of Reasons at 2). Texaco contends that the text of NTL-4A and the comments in the Federal Register notice demonstrate the Department's intent to have NTL-4A retroactively modify and correct the provisions of NTL-4 found invalid in Marathon. Texaco asserts that, to correct the invalid NTL-4 provisions, gas flared between December 1, 1974 (the effective date of NTL-4) and January 1, 1980 (the effective date of NTL-4A) must be retroactively exempted from royalties because NTL-4A retroactively authorized flaring during that period.

In reply MMS argues that the Marathon decision invalidated only those portions of NTL-4 that departed from the Department's long-established practice of not assessing royalties on unavoidably lost or beneficially used gas. According to MMS, the gas flared by Texaco was avoidably lost gas, the Department has always required compensation for avoidably lost gas, and the royalty was properly assessed. According to MMS, since June 2, 1942, the regulations have called for full value payment for wasted (avoidably lost) gas (see, e.g., 30 CFR 221.35 (1979)). 4/ MMS contends that Texaco has failed to show that the flared gas was unavoidably lost or that it had gained permission to flare the gas, and the decision should be affirmed.

[1] The relevant language of NTL-4A provides:

> No royalty obligation shall accrue on any produced gas which * * * (2) is vented or flared with the Supervisor's prior authorization or approval during drilling, completing, or producing operations, (3) is vented or flared pursuant to the rules,

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3/ The BLM response is contained in memoranda dated Oct. 21, 1990, Apr. 1, 1991, Apr. 3, 1991, July 8, 1991, and Aug. 16, 1991.

4/ The pertinent language of 30 CFR 221.35 (1979) is quoted below.

> regulations, or orders of the appropriate State regulatory agency when said rules, regulations, or orders have been ratified or accepted by the Supervisor, or (4) the Supervisor determines to have been otherwise unavoidably lost.
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> Where produced gas * * * is (1) vented or flared during drilling, completing, or producing operations without the prior authorization, approval, ratification, or acceptance of the Supervisor or (2) otherwise avoidably lost, as determined by the Supervisor, the compensation due the United States or the Indian lessor will be computed on the basis of the full value of the gas so wasted, or the allocated portion thereof, attributable to the lease.

We agree with Texaco that NTL-4A was issued to replace the provisions of NTL-4 struck down in the Marathon decision. In its Federal Register notice announcing NTL-4A the Department stated that "[t]he revocation of certain provisions of NTL-4 and its supersession by NTL-4A is necessary to comply with court decisions * * *." 44 FR 76600 (Dec. 27, 1979). The Federal Register notice also stated that "the provisions of NTL-4 superseded by this action are revoked retroactive to December 1, 1974, the effective date of said Notice."

It is equally important that the Marathon decision rejected the portion of NTL-4 which changed the long-standing Departmental policy that a royalty would not be assessed for oil or gas which is unavoidably lost or used in lease operations. The Department's policy before NTL-4 was that it was to be compensated for the full value of avoidably lost gas. The court did not hold this provision in NTL-4 invalid, as it did not deviate from prior policy. NTL-4A provided for reimbursement of royalties assessed on oil and gas that was unavoidably lost or used in lease operations because that oil and gas would not have been subject to a royalty if the policy in effect prior to NTL-4 had been applied. NTL-4A specifically states that the United States will be compensated for the full value of avoidably lost production.

Texaco's claim that NTL-4A retroactively authorized gas flaring is based on the text of section IV.B., paragraph 2, which states:

> The venting or flaring of gas from oil wells completed prior to the effective date of this Notice is authorized for an interim period. However, an application for approval to continue such practices must be submitted within 90 days from the effective date hereof, unless such venting or flaring of gas was authorized, approved, ratified, or accepted previously by the Supervisor. For oil wells completed on or after the effective date of this Notice, an application must be filed with the Supervisor, and approval received, for any venting or flaring of gas beyond the initial 30-day or other authorized test period.

Noting that the first sentence authorizes flaring during an interim period, Texaco argues that the interim period was from December 1, 1974, to January 1, 1980. According to Texaco, the second sentence notifies producers that this authorization would not automatically continue after the effective date of NTL-4A if the flaring has not been previously approved by the Supervisor. It maintains that the second and third sentences address flaring after the effective date of NTL-4A, and the first sentence must relate to the entire period before the effective date.

MMS argues that section IV.B., paragraph 2 is prospective from the effective date of NTL-4A, January 1, 1980. It contends that in "the absence of express language stating that unapproved flaring is retroactively authorized, this clear language cannot be twisted into a retroactive application" (MMS Answer at 7).

If we were to apply Texaco's interpretation, our decision would have one striking similarity to NTL-4. It would be contrary to the Department's long standing policy that it should be compensated for avoidably lost gas. This policy is reflected in 30 CFR 221.35 (1979), in effect during the 1975 - 1977 period, which provided:

> The lessee is obligated to prevent the waste of oil or gas and to avoid physical waste of gas the lessee shall consume it beneficially or market it or return it to the productive formation. If waste or [sic] gas occurs the lessee shall pay the lessor the full value of all gas wasted by blowing, release, escape or otherwise * * *.

The comparable regulation now in effect, 43 CFR 3162.7-1, requires a royalty payment for lost or wasted oil or gas. 5/ The Department has required payment for avoidably lost gas before, during, and after the interim period. Only the method of calculating the amount due has changed.

Additional support for this interpretation can be found elsewhere in NTL-4A and in the Federal Register notice announcing NTL-4A. Section II.A of NTL-4A defines "avoidably lost" production as "the venting or flaring of produced gas without the prior authorization, approval, ratification, or acceptance of the Supervisor and the loss of produced oil or gas when the Supervisor determines that such loss occurred as a result" of some action or failure to act by the lessee or operator.

The Federal Register notice announcing NTL-4A stated that lessees and operators who submitted royalty payments under the revoked provisions

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5/ Under 43 CFR 3160.0-5(b) and NTL-4A, gas which is vented or flared without the prior approval of the authorized officer is deemed to be avoidably lost. 43 CFR 3162.7-1(d) assesses a royalty for avoidably lost gas. In Mobil Exploration & Producing U.S. Inc., 119 IBLA 76 (1991), we held that 43 CFR 3162.7-1(d) would apply retroactively, making the compensation for avoidably lost gas the royalty value rather than full value.

of NTL-4 could apply for a refund. The addendum to NTL-4A sets out the requirements for these applications. 44 FR 77600 (Dec. 27, 1979). After noting the retroactively revoked portions of NTL-4, the addendum states that lessees and operators who submitted royalty payments pursuant to NTL-4 could apply for a refund of

> those payments made for (1) oil that was unavoidably lost or used for beneficial purposes on the lease, communitized tract, or unitized participating area from which it was produced and/or (2) gas that was vented or flared with the prior approval of the Supervisor or unavoidably lost. * * * [N]o refunds will be made of those payments submitted on the basis of a determination of waste by the Supervisor. [Emphasis supplied.]

Id. at 76601. Thus, the addendum, which provides for refund of payments made pursuant to the provisions of NTL-4, specifically excludes royalties paid for gas that was flared without prior approval or avoidably lost.

Texaco did not gain prior approval for flaring the gas, and there is no basis in the record for holding that the flared gas was unavoidably lost. MMS made repeated requests for evidence that approval for flaring had been granted or that the gas was unavoidably lost, but Texaco submitted nothing. NTL-4A reinstated the long standing policy of the Department.
It did not change the pre-NTL-4 policy that the Government should be compensated for gas that was flared without permission and avoidably lost gas.

Accordingly, pursuant to the authority delegated to the Board of Land Appeals by the Secretary of the Interior, 43 CFR 4.1, the decision appealed from is affirmed.

R. W. Mullen
Administrative Judge

I concur:

Bruce R. Harris
Deputy Chief Administrative Judge